92-1382

No.——

Supreme Court, U.S.
FILED
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

CAPTRAN CREDITORS' TRUST, CLUB BAHA, LTD. and TROPICAL PROPERTIES, LTD.,
Petitioners,

v.

DAVID W. MCCONNELL, GERARD A. MCHALE, JR. and MCHALE, EZZELL & CO., P.A.,
Respondents.

Petition for Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

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PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Is it against federal public policy for trustees in a federal bankruptcy proceeding, including a certified public accountant, to be insulated from liability for willful breaches of their fiduciary duties by a Trust Agreement clause allowing recovery only for "proven dishonesty"?

PARTIES TO THE PROCEEDINGS

Petitioner and Plaintiff-Appellant below, Captran Creditors' Trust, is a Trust organized under the laws of the State of Florida. Petitioner and Plaintiff-Appellant below, Club Baha, Ltd., is a non-publicly traded holding company organized under the laws of the Bahamas. Pursuant to Supreme Court Rule 29.1, petitioners note that Club Baha, Ltd. is a wholly owned subsidiary of Tropical Properties, Ltd.

Respondents and Defendant-Appellees below are David W. McConnell, Gerard McHale, Jr., and McHale, Ezzell & Co., P.A.

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CAPTRAN CREDITORS' TRUST, CLUB BAHA, LTD.
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DAVID W. MCCONNELL, GERARD A. MCHALE, JR.
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Respondents.

Petition for Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

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PETITION FOR WRIT OF CERTIORARI

Petitioners, Captran Creditors' Trust, Club Baha, Ltd., and Tropical Properties, Ltd., respectfully pray that this Court issue a Writ of Certiorari to review the judgment and opinion of the United States Court of Appeals for the Eleventh Circuit entered on November 10, 1992.

OPINIONS BELOW

The opinion of the Eleventh Circuit Court of Appeals affirming the decision of the United States District Court for the Middle District of Florida is not officially re-

ported and is reprinted in the appendix hereto ("App.") at 1a. The opinion of the District Court, which affirmed the decision of the United States Bankruptcy Court, is not officially reported and is reprinted at App. 2a. The Bankruptcy Court's opinion denying the relief sought by petitioners is not officially reported and is reprinted at App. 20a.

JURISDICTION

Jurisdiction in the Bankruptcy Court was based upon provisions of the Captran Creditors' Trust Agreement, which arose from a Plan of Reorganization approved on June 13, 1988. The Bankruptcy Court entered its Findings of Fact, Conclusions of Law and Memorandum Opinion on April 14, 1990, and a final judgment was entered on April 17, 1990. Petitioners filed a timely notice of appeal in the United States District Court for the Middle District of Florida on April 27, 1990, and the District Court affirmed the judgment on June 17, 1991. Petitioners filed a timely notice of appeal to the United States Court of Appeals for the Eleventh Circuit, which affirmed the lower court's decision on November 10, 1992. The jurisdiction of this Court to review the judgment below is invoked under 28 U.S.C. § 1254(1).

PERTINENT STATUTORY PROVISIONS

None.

STATEMENT OF THE CASE

A. Factual Background

Petitioners Club Baha, Ltd. and Tropical Properties, Ltd. obtained a $1.7 million final judgment in Fort Myers, Florida Circuit Court against Captran Resorts International (CRI) based on CRI's violation of escrow requirements, breaches of fiduciary duties, and misrep-

resentations or concealment.[1] CRI was owned and/or controlled by Keith Trowbridge. In order to avoid payment of the judgment, CRI filed for Chapter 11 bankruptcy protection. During the bankruptcy, the "Captran Creditors' Settlement Agreement" was signed, which created a Trust to receive, liquidate and distribute CRI's assets[2] to the CRI creditors/Trust beneficiaries. Respondent Gerard McHale, Jr. negotiated the Agreement for Petitioner Club Baha and had direct input into its preparation and drafting. This Agreement also created Petitioner Captran Creditors' Trust (CCT), which was to acquire the majority of CRI's assets. The trust was created solely to take CRI assets out of its control.

Respondents McHale, a Certified Public Accountant (CPA), and David McConnell, an attorney, were appointed Trustees. McHale was simultaneously engaged as a CPA by Club Baha, thus becoming a co-trustee, and continuing to act as a CPA, on Club Baha's behalf. Respondent McHale, Ezzell & Company (M.E.C.) was an accounting firm owned by McHale and retained by Club Baha to perform services in connection with the Trust. CCT acquired specific assets from CRI and assumed only those liabilities listed in the Contract for Purchase. The assets were marketed and sold. Club Baha, the largest beneficiary, never received any proceeds at all; they instead went to CRI.

Sales of Trust properties were made through a real estate firm owned and controlled by Trowbridge, and

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[1] Respondent-Trustee, Gerard McHale, Jr. (McHale) was Club Baha's expert accountant witness at the trial against CRI. He filed a "special report" in those proceedings detailing alleged wrongs committed by CRI.

[2] The trust assets included 1400 timeshare unit weeks at five different resort properties, undeveloped land, two mortgage loan reserve portfolios, and a promissory note. These assets were valued by the Trustees in the Trust Agreement at approximately $6,800,000.

they were processed through his title company. Trust property sales records were under the exclusive control of CRI's controller, George Mills, and the trial court found that McHale accepted his recordkeeping without question or verification, and that neither McHale nor McConnell kept any sales records.

Although the Trust was created for the specific purpose of liquidating the Trust assets, respondents allowed CRI to continue to develop and build on undeveloped properties conveyed to the Trust. As the trial court found, the record left no doubt that the Trustees agreed to this activity.

The Trustees were discharged in August 1984, and McHale submitted his final report. As the trial court found:

> By all accounts, this report did not even come close to being an acceptable final accounting of a trustee, and it did not pretend to be one. The report was nothing more than a compilation of the Trust assets and the beneficiary interests that existed at the time the Trust was created; it did not reflect what really existed when McHale's Trusteeship ended. [App. 25a.]

The Petitioners filed an adversary proceeding Complaint for the Trustees' breaches of their fiduciary duties, for the professional negligence of McHale and M.E.C., and for Florida Statutes Chapter 772 violations. McHale and M.E.C. raised defenses, while McConnell was defaulted for failing to file an Answer or make any further appearances in the case.

The allegations in the Amended Complaint were tried in a non-core suit to the Bankruptcy Court, which issued its Memorandum Opinion in 1990. The court reviewed volumes of evidence demonstrating departures from trustee norms, variations from and breaches of duties, and violations of a CPA's duty of care to his client, Club Baha.

The evidence at trial showed that among the breaches by the Trustees were the following:

- Letting CRI sell Trust assets and mortgage reserve assets at "fire sale" values.[3]
- Letting CRI keep Trust proceeds.
- The payment of illegal and unearned commissions to CRI, an unlicensed realtor, on sales that had not closed (in violation of Chapter 475, Florida Statutes).[4]
- Allowing cash assets that should have been paid to CCT beneficiaries to be "laundered" back to CRI.
- Letting CRI develop Trust property, contrary to the stated purpose of the Trust.
- Not complying with state Regulations.
- Letting untimely claimants opt in as Trust creditors.

Evidence also demonstrated that the wasting of trust assets was secreted by:

- Not maintaining Trust records.
- Not terminating in a timely fashion the CRI marketing arrangement.

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[3] The General Electric Credit Corporation loan portfolio was valued at $752,293 on November 19, 1982, in the Trust Agreement itself, the drafting of which McHale participated in. Shortly after the valuation, McHale sold the loan portfolio for $17,000 cash. Trial Tr. pp. 293, 294, 301.

[4] McHale prepaid 38% commissions to CRI on unit sales that had not closed even though the Trust Agreement explicitly called for payment of commissions upon closing only. Trial Tr. pp. 277, 278. In addition, CRI was not licensed to sell timeshare interests as required by Florida Statutes Chapter 475. McHale made no attempt to verify CRI's status as it related to timeshare sales and, in fact, acquiesced in the payment of commissions to a non-real estate broker.

- Not providing an Annual Accounting.
- Letting a competing interest "ghostwrite" the Final Accounting.
- Distributing a deficient and misrepresentative Final Accounting.

The trial court, although at one point stating that McHale's performance did not fall below CPA standards, made a series of factual and legal conclusions that respondents' actions—whether judged by attorney or CPA standards, or simply by those applicable to ordinary Trustees—fell well below what the law demands of fiduciaries. For example:

> . . . [T]here is no doubt that McHale accepted the recordkeeping of Mills without question or without verification. [App. 23a.]
>
> * * * *
>
> [The] [e]vidence . . . leaves no doubt that neither McHale nor McConnell kept any records regarding the sales transactions. . . . [*Id.*]
>
> * * * *
>
> [McHale and McConnell] simply let Trowbridge and [Trowbridge's title company] handle all details regarding the sales and recordkeeping of CRI. [*Id.*]
>
> * * * *
>
> The record leaves no doubt that the Trustees agreed, at least tacitly, to [CRI's continued development activity] and at no time voiced objection to it. [*Id.*]
>
> * * * *
>
> By all accounts, this report [McHale's final accounting] did not even come close to being an acceptable final accounting of a Trustee, and it did not pretend to be one. [App. 25a.]
>
> * * * *
>
> This record leaves no doubt that the conduct of McHale as a Trustee certainly left a lot to be desired. . . . [App. 26a.]

> [McHale's] detached, lackadaisical attitude toward the Trust affairs may be charitably characterized at most as benign neglect. [*Id.*]
>
> * * * *
>
> McHale's lack of involvement with the Trust was clearly evidenced by his unquestioned acceptance of the Mills Report as a final accounting of his Trusteeship. [*Id.*]
>
> * * * *
>
> [I]t is clear from the record that McHale granted almost a complete free reign to Trowbridge, Mills and [Trowbridge's title company] involving sales of trust assets, sales closings, and the recordkeeping of the Trust assets. [*Id.*]
>
> * * * *
>
> [I]f McHale's performance is measured by the standard of a CPA who was engaged to serve in that capacity, one would be hard pressed to conclude that his performance met the standards of a reasonable CPA. [App. 26a.]
>
> * * * *
>
> . . . McHale might have acted beneath the standard of sound business practices. . . . [App. 28a.]

The reason the trial court did not have to decide finally whether respondents breached their fiduciary duties —despite the findings outlined above—is that in any event they were exculpated by a clause in the Trust Agreement which read: "Except for proven dishonesty, a Trustee will not be personally liable for any act or omission in connection with his duties as Trustee." [5]

Thus, the trial court stated its satisfaction that "although McHale might have acted in a less than professional manner and may possibly have acted beneath the

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[5] The Bankruptcy Court effectively adopted and enforced the Trust Agreement in a series of orders. *E.g.*, Order of Dismissal of Bankruptcy Proceedings, Dec. 6, 1982; Order Approving Sale of Assets, Dec. 6, 1982. See also App. 22a, 27a-28a.

standard of sound business practices, he was not dishonest." App. 28a.[6]

Petitioners appealed to the Federal District Court for the Middle District of Florida pursuant to 28 U.S.C. § 158. The District Court, while not disturbing the underlying facts found by the Bankruptcy Court, apparently misunderstood that court's legal conclusions. The District Court thought the Bankruptcy Court had held in the alternative that petitioners had failed to carry their burden of proving violations of fiduciary duties *and* that, in any event, respondents were exonerated by virtue of the exculpatory "dishonesty" clause in the Trust Agreement. The District Court therefore affirmed. Perhaps under the same misunderstanding, the Eleventh Circuit affirmed without opinion.

REASONS FOR GRANTING THE WRIT

This case presents a serious question of federal public policy that goes to the very heart of bankruptcy law and of fiduciary trustee duties generally. The Bankruptcy Court clearly found that the Trustees in this case displayed "detached, lackadaisical" attitudes toward their duties, granted complete reins of power to others (including those owned and controlled by the bankrupt party), exhibited "benign neglect" instead of the required heightened duty of care, and generally conducted themselves in a manner that "left a lot to be desired."

Yet they were held to be exempt from normal standards because of an exculpatory clause relating to outright dishonesty. Giving commanding effect to this clause allows fiduciaries to behave in the most outrageous manner short of what the Bankruptcy Court deemed to be self-dealing

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[6] There is no evidence in the record that the beneficiaries ever specifically discussed the meaning or intent of the "proven dishonesty" exculpation clause with anyone, including but not limited to their legal or accountant representatives.

or profit-taking from the bankrupt estate. Thus, the Trustees can wholly ignore their duties, carry them out in a way that conflicts with the interests of the creditors and other Trust beneficiaries, engage in speculative and nonmeritorious ventures, allow others to profit at the Trust's expense, and perform a host of other all-but-illegal acts—without being held to account. Such a result, we submit, so egregiously counters the public interest that this Court's supervisory power over the federal courts is called into play.

This Court has made clear that under traditional equity principles, "a trustee bears an unwavering duty of complete loyalty to the beneficiary of the trust, to the exclusion of the interests of all other parties," and "the rule against a trustee dividing his loyalties must be enforced with 'uncompromising rigidity.'" *NLRB* v. *Amax Coal Co.*, 453 U.S. 322, 329-330 (1981) (citation omitted). "[F]iduciaries owe their beneficiaries a duty of care as well as a duty of loyalty. . . ." *Air Line Pilots Ass'n* v. *O'Neill*, 111 S. Ct. 1127, 1134 (1991).[7]

Violation of a trust relationship—which clearly occurred in this case—is so serious as to warrant even the imposition of a constructive trust on the earnings from the publication of otherwise protected First Amendment materials. *Snepp* v. *United States*, 444 U.S. 507, 510, 515 (1980). And damages are an appropriate remedy. Even the United States has been held liable once it was established that it occupied the position of trustee and had acted improperly in its fiduciary relationship. *United States* v. *Mitchell*, 463 U.S. 206, 224-228 (1983).[8] "It is well established that

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[7] Thus, ERISA provides for personal liability for a fiduciary who breaches "any of the responsibilities, obligations, or duties imposed upon fiduciaries by this title." 29 U.S.C. § 1109(a); *see Massachusetts Mut. Life Ins. Co.* v. *Russell*, 473 U.S. 134 (1985).

[8] *See also Nevada* v. *United States*, 463 U.S. 110, 142 (1983). *Cf. United States* v. *Mitchell*, 445 U.S. 535, 540-546 (1980). The

a trustee is accountable in damages for breaches of trust." *Id.* at 226.

Not so here. Respondents engaged in a variety of breaches of the trust imposed upon them, but they have been held *not* accountable by reason of one sentence in an agreement devised by the parties. The opposite rule is the applicable one. *See Firestone Tire & Rubber Co.* v. *Bruch*, 489 U.S. 101, 111 (1989).

If the ruling below stands, a bankruptcy trustee—or any other trustee—could use the processes of a federal court to perpetrate a fraud, so long as he was careful not to overstep the line into outright dishonesty. He could, for example, improperly exclude property from the estate, *cf. United States* v. *Whiting Pools, Inc.*, 462 U.S. 198, 203 (1983); deliberately favor one creditor over another, *cf. Railway Labor Executives' Ass'n* v. *Gibbons*, 455 U.S. 457, 469 (1982); intentionally deny a creditor postpetition interest on a nonconsensual oversecured claim, *cf. United States* v. *Ron Pair Enters.*, 489 U.S. 235 (1989); wrongfully waive a bankrupt corporation's attorney-client privilege, *cf. Commodity Futures Trading Comm'n* v. *Weintraub*, 471 U.S. 343, 355 n.7 (1985); willfully minimize rather than maximize the value of an estate, *see id.* at 352; carry out his duties under a clear and direct conflict of interest, *cf. Firestone Tire & Rubber Co.* v. *Bruch*, 489 U.S. 101, 115 (1989); purposely give an unfair and incomplete review of claim denials instead of the full and fair review that is required, *cf. id.* at 113; or even knowingly engage in sham or collusion, *cf. Navarro Sav. Ass'n* v. *Lee*, 446 U.S. 458, 465 (1980). He could do all of this because he was not acting dishonestly under the Bankruptcy Court's definition.

The courts below effectively turned over to the parties the determination not only of the Trustees' duties but the standards by which their conduct must be judged. Yet

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United States, as trustee, must "exercise great care" in administering its trust. *United States* v. *Mason*, 412 U.S. 391, 398 (1973).

it is precisely this reasoning that was rejected by this Court in *Firestone Tire & Rubber Co.* v. *Bruch*, 489 U.S. at 112, where the Court said:

> As they do with contractual provisions, courts construe terms in trust agreements without deferring to either party's interpretation. "The extent of the duties and powers of a trustee is determined by the rules of law that are applicable to the situation, and not the rules that the trustee or his attorney believes to be applicable, and by the terms of the trust *as the court may interpret them*, and not as they may be interpreted by the trustee himself or by his attorney." 3 W. Fratcher, Scott on Trusts § 201, at 221 (emphasis added).

This is a recognition that more than private interests are at stake. If a trustee is allowed to roam at will, harnessed only by the gauge of dishonesty, the public trust as well as private interests are compromised, legal principles are belittled, and faith in the rule of law is diminished in the eyes of those it serves.

If we turn to state law for guidance,[9] the result is the same.

Following the lead of Justice Cardozo for the New York Court of Appeals as early as 1928, state courts have adopted an "unbending and inveterate, [u]ncompromising rigidity" toward the duty of trustee fiduciaries, demanding not only honesty "but the punctilio of honor." *Meinhard* v. *Salmon*, 164 N.E. 545, 546 (N.Y. 1928) (cited with approval by this Court in *NLRB* v. *Amax Coal Co.*, 453 U.S. at 329-330). They have followed the general rule that trustees must act in good faith, use reasonable

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[9] This Court has pointed out that a trustee's powers under the Bankruptcy Code are limited by a judicially developed doctrine intended to protect legitimate state interests, so that a trustee, for example, cannot abandon trust property in contravention of local law designed to protect public health and safety. *Midatlantic Nat'l Bank* v. *New Jersey Dep't of Envtl. Protection*, 474 U.S. 494, 500-506 (1986). *See also Butner* v. *United States*, 440 U.S. 48 (1979).

judgment, deal impartially with beneficiaries of the Trust, and exercise the care, skill and judgment of the ordinarily prudent person.[10] If the trustee has greater skills—as the attorney and CPA did in this case—they must exercise these greater skills.[11] Even a grant in a Trust Deed of absolute discretion does not authorize a trustee to neglect his trust or abdicate his judgment, which will be subject to judicial review.[12]

Exculpatory clauses in trust agreements are disfavored and are not enforced as to breaches of the trust committed in bad faith, intentionally, or with reckless indifference to the interests of the beneficiaries.[13] Exculpatory clauses have, in fact, been held void in the State involved here, Florida, because they attempted to immunize a party from the effects of his own fraud.[14]

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[10] *E.g., Eddy* v. *Colonial Life Ins. Co. of Am.*, 919 F.2d 747, 750-751 (D.C. Cir. 1990) (and cases there cited); *MCA Inc.* v. *United States*, 685 F.2d 1099, 1103 (9th Cir. 1982) (applying California law); *see duPont* v. *Southern Nat'l Bank of Houston*, 771 F.2d 874, 888 (5th Cir. 1985) (applying Texas law), *cert. denied*, 475 U.S. 1085 (1986).

[11] *E.g., Pension Benefit Guar. Corp.* v. *Greene*, 570 F. Supp. 1483, 1492-93 (W.D. Pa. 1983) (applying Pennsylvania law), *aff'd*, 727 F.2d 1100 (3d Cir.), *cert. denied*, 469 U.S. 820 (1984).

[12] *MCA Inc.* v. *United States*, 685 F.2d at 1103.

[13] *See, e.g., Dill* v. *Boston Safe Deposit & Trust Co.*, 175 N.E.2d 911, 913 (Mass. 1961) (and authorities there cited); *Wenzel* v. *Boyles Galvanizing Co.*, 920 F.2d 778, 781 (11th Cir. 1991) (applying Florida law); *University Plaza Shopping Center, Inc.* v. *Stewart*, 272 So.2d 507, 511-512 (Fla. 1973) (in Florida, any indemnity must be clear and explicit, and must cover every contingency); *Nat Harrison Assocs.* v. *Florida Power & Light Co.*, 162 So.2d 298, 299 (Fla. Dist. Ct. App. 1964), *cert. denied*, 166 So.2d 754 (Fla. 1964); *Bogert Trusts* § 542.

[14] *E.g., Zuckerman-Vernon Corp.* v. *Rosen*, 361 So.2d 804, 806 (Fla. Dist. Ct. App. 1978); *Fuentes* v. *Owen*, 310 So.2d 458, 459-460 (Fla. Dist. Ct. App. 1975) (including cases in other States).

Thus, the result below violates virtually every canon of trust law established by the federal and state courts. The exculpatory clause was favored and given all-encompassing meaning; it was not held void but, on the contrary, enforced to its full limit; instead of requiring good faith and reasonable judgment, the lower courts permitted every conceivable degree of mismanagement and culpability except outright dishonesty; and trustees with special skills were treated no differently than ordinary laymen.

This last point requires emphasis. McConnell, of course, was a Trustee attorney and an officer of the court. The beneficiaries had a right to assume on his part not only special skills and an added duty of care but an adherence to legal principles. McHale was a CPA who, from the outset, had divided loyalties and represented himself to the Petitioner beneficiaries as a professional looking out for their complex financial interests. If specialists such as Respondents McConnell and McHale are allowed to act in any manner they please short of stealing, the federal courts will have become a party to public policy violations of the highest order.

CONCLUSION

For each and all of the reasons above, the petition should be granted and the judgment below reversed.

Respectfully submitted,

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APPENDICES

APPENDICES

APPENDIX A

IN THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

No. 91-3686

D.C. Docket No. 90-719-CIV-T-17A

IN RE: CAPTRAN CREDITORS' TRUST,
Debtor.

CAPTRAN CREDITORS' TRUST, CLUB BAHA, LTD., and
TROPICAL PROPERTIES, LTD.,
Plaintiffs-Appellants,

versus

DAVID W. MCCONNELL, JR., GERARD A. MCHALE, and
MCHALE, EZZELL & CO., P.A.,
Defendants-Appellees.

Appeal from the United States District Court
for the Middle District of Florida

(November 10, 1992)

Before TJOFLAT, Chief Judge, EDMONDSON, Circuit Judge, and DYER, Senior Circuit Judge.

PER CURIAM:

AFFIRMED. *See* 11th Cir. R. 36-1.

APPENDIX B

UNITED STATES DISTRICT COURT
MIDDLE DISTRICT OF FLORIDA
TAMPA DIVISION

Case No. 90-719-CIV-T-17(A)

IN RE: CAPTRAN CREDITORS' TRUST,
Debtor.

CAPTRAN CREDITORS' TRUST, CLUB BAHA, LTD., a foreign corporation and TROPICAL PROPERTIES, LTD., a foreign corporation,
Appellants,

vs.

DAVID W. MCCONNELL, GERARD A. MCHALE, JR., and MCHALE, EZZELL AND CO., a Florida professional association,
Appellees.

Appeal from the United States Bankruptcy Court
for the Middle District of Florida

[Filed June 17, 1991]

This cause is before the Court on appeal from the Final Judgment of the Bankruptcy Court entered in this adversary proceeding in favor of appellees. Chief Bankruptcy Judge Alexander L. Paskay entered Final Judgment on April 17, 1990 upon the Findings of Fact, Conclusions of Law and Memorandum Opinion dated April 4, 1990.

STANDARD OF APPELLATE REVIEW

Findings of fact by the Bankruptcy Court will not be set aside unless clearly erroneous. Bankruptcy Rule 8013; *In re Downtown Properties, Ltd.*, 794 F.2d 647 (11th Cir. 1986). However, appellants are entitled to an independent, *de novo* review of all conclusions of law and the legal significance accorded to the facts. *In re Owens*, 86 B.R. 691 (M.D. Fla. 1988).

FACTS

1. In 1982, Captran Resorts International, Inc. (CRI), a corporation based in Lee County, Florida, was engaged in the business of developing resorts and selling timeshare interests to the public. CRI's president was Keith Trowbridge (Trowbridge).

2. CRI, through its president Trowbridge, entered into a joint venture with Club Baha, Ltd. (Club Baha) and Tropical Properties, Ltd. (Tropical Properties). Tropical Properties is the parent organization of Club Baha, its wholly owned subsidiary. Jack Grobowsky (Grobowsky) controlled Tropical Properties which developed resorts and timeshare interests in the Bahamas.

3. The CRI joint venture with Club Baha resulted in a disagreement and litigation between the parties. Club Baha sued CRI and it's president, Trowbridge, asserting fraud and breach of contract involving the development and marketing of a Club Baha timeshare resort in the Bahamas. A lengthy jury trial was held in the Circuit Court for Lee County, Florida. On May 18, 1982 Club Baha obtained a $1.7 million dollar final judgement for compensatory and punitive damages against CRI and Trowbridge.

4. CRI could not pay the $1.7 million Club Baha judgment lien and continue its resort development and timeshare business. Further, CRI could not post a supersedeas bond to avoid losing some, if not all, of its property.

5. On July 16, 1982, CRI filed a voluntary Petition for Relief under Chapter 11 of the Bankruptcy Code. Soon thereafter, CRI and some of its largest creditors, including Club Baha and Tropical Properties, entered into extensive negotiations. The purpose of their negotiations was to ultimately satisfy CRI's creditors and to resolve CRI's problems outside of the provisions of Chapter 11 and the Bankruptcy Court.

6. The negotiations resulted in the "Captran Creditors' Settlement Agreement" (Trust Agreement) which provided that the CRI creditors would form the Captran Creditors' Trust (CCT or Trust). It was later ruled that the Captran Creditors' Trust constituted a business trust under section 101(8) of the Bankruptcy Code. *In re Captran Creditors' Trust*, 53 B.R. 741 (Bankr. M.D. Fla. 1985). A copy of the Trust Agreement, a synopsis of its development, and copies of related documents are included in what is referred to as "the yellow book".

7. Appellants allege that appellee McHale negotiated the Trust Agreement for Club Baha. Appellees counter that McHale did not negotiate the agreement for Club Baha. Moreover, appellees contend that Domenic Massari (Massari), appellants' attorney, was instrumental in drafting the Trust Agreement as well as being the chief architect of the legal structure of the Trust. Appellees add that according to Grobowsky, Massari was the major author of the Trust Agreement. In their briefs, appellants do not refute that Massari authored the Trust Agreement.

8. The Trust Agreement was finalized in December, 1982. Based on the settlement, the Bankruptcy Court on December 6, 1982 entered an order granting CRI's motion to dismiss its Chapter 11 case. The Trust was effective following the final agreement.

9. CRI assets, and any debts and liabilities of those assets, including 1400 timeshare unit weeks at five different resort properties; undeveloped land; two mortgage portfolios and a promissory note, were transferred to the CCT to be the Trust res. CRI creditors were to be the CCT beneficiaries. Appellees McConnell, an attorney, and McHale, a Certified Public Accountant (Trustees), were appointed as initial trustees of CCT. CRI retained a residual interest in the CCT properties, if one remained after the liquidation of the Trust assets and after the satisfaction of the interests of the Trust beneficiaries.

10. Appellees McConnell and McHale were both familiar with the parties' businesses before appointment as Trustees. McConnell had significant business dealings with CRI and Trowbridge during the CRI bankruptcy. He was considered closely aligned with CRI and Trowbridge. McHale had previously been retained by Club Baha for financial and economic analysis during its litigation with CRI and Trowbridge. He was considered closely aligned with Club Baha and Grobowsky. CRI and the CCT beneficiaries sought to balance their competing interests by appointing these Trustees to administer the Trust.

11. A major asset of the CCT was the land of Sanibel Island Beach Club (SIBC), a phased development having multiple buildings upon completion. Building 10 was almost built however it was not certified for occupancy. The Trust owned the land for Buildings 8 and 9. CRI had building permits for Buildings 8 and 9 from before the commencement date of the Trust. The land for Buildings 5, 6, and 7 was also a Trust asset but no building permits had yet been issued. Appellees claim the building permits for Buildings 8 and 9 would have been lost had construction not commenced. Appellant Club Baha, and Growbowsky, claim that they were unaware that CRI had building permits for Buildings 8 and 9. The CCT and CRI were, in affect, dependent on each other concerning the SIBC development.

12. The CRI assets transferred to the CCT were to be marketed and sold. Net sales proceeds were to go to the Trust for the benefit of the Trust beneficiaries. Under the Trust Agreement, CRI was to act as the marketing agent for the CCT properties. In exchange, CRI would receive a 38% marketing fee based on the sale price of the properties it sold. The Trust Agreement allowed the CCT properties to be sold at a 10% discount. Discounts above 10% were deducted from CRI's 38% marketing fee with the Trust always getting 62% of the net sales proceeds. CRI acted as the marketing agent for the CCT properties.

13. Actual sales of the CCT property were handled by a real estate firm owned and controlled by Trowbridge. Northern American Title Insurance Agency, Inc. (NATIA), also owned and controlled by Trowbridge, processed the sales, handled closings, and maintained the records regarding the sales of timeshare unit weeks. All sales records of the Trust properties were under the exclusive control of George Mills (Mills), CRI's controller.

The Trustees received weekly sales reports on Trust inventory, monthly schedules of closed sales, monthly balances in escrow, cumulative showings of use of escrow funds for development and construction purposes, escrow draw approvals and draw requests from the construction company. In addition, the Trustees met approximately bi-weekly with Mills.

14. The Trust Agreement stated the purpose of the Trust as follows:

> Purpose: This Trust is organized for the primary purpose of liquidating the assets transferred to it with no objective to continue or engage in the conduct of a trade or business.

The Trust Agreement also had a provision regarding Trustee liability. It stated:

> Trustee Liability: Except for proven dishonesty, a Trustee shall not be personally liable for any act or omission in connection with his duties as Trustee.

As noted above, the Trust Agreement was the product of the parties after extensive negotiations.

15. In 1983, CRI continued developing Buildings 8 and 9 at SIBC. The land for those Buildings was a Trust asset to be liquidated under the stated purpose of the Trust Agreement. The Trustees agreed, at least tacitly, to this activity by CRI, and at no time voiced any objection to it. On the contrary, appellee McHale consented to this development believing it would maximize the return to the Trust beneficiaries. Grobowsky first learned that Buildings 8 and 9 were being developed in July, 1983. It appears that even though the Trust Agreement did not authorize any additional development, the effect of developing Buildings 8 and 9 resulted in a net benefit to the Trust of $1.7 million dollars.

16. In 1983 the Trustees and Grobowsky both tried selling the CCT assets in bulk. No buyer was found. Next, Club Baha suggested that CCT assets be liquidated to the Trust beneficiaries. The Trustees developed a liquidation plan to distribute the Trust assets in-kind to the CCT beneficiaries. In exchange, the Trust beneficiaries would extinguish their interests in the Trust.

17. CRI, in the Fall of 1983, resisted the in-kind distribution plan and threatened to sue the Trustees if they proceeded with the plan. CRI resisted the plan because it held a residual interest in the Trust properties.

18. In February, 1984 the Trustees filed a suit for declaratory relief requesting that the Circuit Court for Lee County, Florida approve the in-kind distribution. Furthermore, the Trustees sought a temporary restraining order to remove CRI as the marketing agent for the CCT assets. The temporary restraining order was denied. The in-kind distribution plan never materialized.

19. During the pendency of the declaratory suit in the Circuit Court for Lee County, several of the CCT beneficiaries assigned their Trust interest to Club Baha. As a result, Club Baha, controlled by Grobowsky, held over 90% of the beneficial interest of the Trust.

20. On August 27, 1984, Grobowsky, as president of Club Baha and Tropical Properties, and on behalf of 90% of the Trust beneficiaries, discharged McHale and McConnell from their duties as Trustees. At that time, the Trust had $1,824.00 in cash; $346,268.00 cash in escrow awaiting release of Grobowsky's lien to close; $972,089.00 in mortgage notes receivable awaiting release of Grobowsky's lien to close; ninety-six timeshare unit weeks at SIBC and four hundred eighty-five timeshare unit weeks in other timeshare resorts. Successor Trustees were appointed.

21. On August 30, 1984, the successor Trustees reached an agreement between Club Baha and the Trust. Their agreement provided that the new Trustees would transfer the bulk of the CCT assets to Club Baha in exchange for Club Baha's interest in the Trust. Throughout the Fall of 1984, Club Baha and the successor Trustees made final plans to execute the agreed upon exchange.

22. In October, 1984, McHale submitted the final accounting of his Trusteeship. The report that McHale submitted was prepared by Mills, CRI's controller. The report was a poor final accounting, merely compiling the Trust assets as they existed when the Trust was created.

23. On January 9, 1985, parties claiming to be CCT creditors filed an involuntary bankruptcy petition against the Trust. That filing held up the plans to transfer the CCT assets to Club Baha. In October, 1985, Judge Paskay ruled that the Captran Creditors' Trust was a business trust and as such it could in fact file for bankruptcy. *In re Captran Creditors' Trust*, 53 B.R. 741 (Bankr. M.D. Fla. 1985). On June 26, 1986, CCT consented to entry of

an order converting the case to a voluntary Chapter 11. Next, Club Baha and Grobowsky proposed a total liquidation plan as the Plan of Reorganization. That plan was confirmed resulting in an in-kind distribution of the CCT assets to the Trust beneficiaries. That in-kind distribution plan was very similar to the one originally planned by McConnell and McHale.

24. On May 7, 1987, appellants filed a three-count Complaint against the appellees. Count I sought compensatory and punitive damages against McConnell and McHale for alleged breach of their fiduciary duties. In Count II, appellants sought compensatory and punitive damages for professional negligence by McConnell and McHale. In Count III, appellants sought damages and other relief from appellees McConnell, McHale, and McHale, Ezzell, and Co., P.A. (MEC) for their alleged violations of Section 772 of the Florida Statutes.

25. McConnell failed to timely file an answer to appellants' Complaint. A Clerk's default was entered against McConnell. Subsequently, appellants filed a three-count Amended Complaint against appellees. Appellants claim in Count I was based on the contention that McHale, in his representative capacity as co-Trustee, breached his fiduciary duty to the Trust beneficiaries. In Count II, appellants caimed that McHale was liable for damages which appellants allegedly incurred as a result of McHale's purported negligence as a CPA. Count III was the same as Count III in the initial Complaint.

26. Appellants claim that Club Baha's alleged damages through December, 1990 are $2.960,859.30. In addition, they allege that the Trust suffered total damages of $3,267,965.00. Appellees refute the alleged damages, charging that the appellants failed to prove that a breach occurred or that any breach proximately caused their alleged injury. Further, appellees contend that appellants have not proffered evidence to support their damage claims

and an exculpatory clause relieves the Trustees of any personal liability.

27. During 1988 and 1989, the Bankruptcy Court held many evidentiary hearings on this dispute. The parties submitted their final arguments in early 1990. Final Judgment was entered on April 17, 1990 in favor of the appellees on Counts I and II of appellants' Complaint. Count III of the appellants' Complaint was dismissed after the final evidentiary hearing. In addition, the Bankruptcy Court withheld entering a final judgment against McConnell who had earlier defaulted.

28. The Bankruptcy Court held that McHale did not breach his fiduciary duties as Trustee of the CCT. The Court also held that the exculpatory clause in the Trust Agreement was not against public policy. It concluded that McHale was not a dishonest Trustee; thus, he would not be personally liable for his activities as Trustee under the exculpatory clause of the Trust Agreement.

The Court based its conclusions on the appellants failure to prove breach of duty and dishonesty as well as upholding the exculpatory clause in the Trust Agreement. The Court withheld entering Final Judgment against McConnell because the appellants offered no meaningful evidence about his conduct as co-Trustee.

ISSUES

I. WHETHER THE PROFESSIONAL TRUSTEES BREACHED THEIR FIDUCIARY DUTIES UNDER THE TRUST AGREEMENT DIRECTLY RESULTING IN INJURY TO THE APPELLANTS.

II. WHETHER THE COURT SHOULD ENTER A FINAL DEFAULT JUDGMENT AGAINST McCONNELL WHERE A DEFAULT WAS ALREADY ENTERED AGAINST HIM AND WHERE HE BREACHED HIS FIDUCIARY DUTIES AS ATTORNEY/TRUSTEE DIRECTLY RESULTING IN INJURY TO THE APPELLANTS.

III. WHETHER McHALE AND McHALE, EZZELL, & COMPANY P.A., OWED A CPA DUTY OF CARE TO THE APPELLANTS WHICH WAS BREACHED AND WHICH DIRECTLY RESULTED IN INJURY.

DISCUSSION

I. THE TRUSTEES DID NOT BREACH THEIR TRUST AGREEMENT FIDUCIARY DUTIES TO THE TRUST BENEFICIARIES. MOREOVER, HAD A BREACH OCCURRED, THE TRUST AGREEMENT ESTABLISHES PROVEN DISHONESTY AS THE ONLY BASIS FOR TRUSTEE LIABILITY.

The Court must consider whether the Bankruptcy Court erred in deciding that the Trustees did not breach their duty. Florida law is well settled concerning the duties and liabilities of trustees.

Two Florida Statutes specifically address the general duties of trustees and their standard of care and performance.

Section 737.301, *Florida Statutes*, states:

> Except as specifically provided, the general duty of the trustee (is) to administer a trust diligently for the benefit of the beneficiaries. . . .

Section 737.302, *Florida Statutes*, addresses a trustee's standard of care and performance as follows:

> Except as otherwise provided by the trust instrument, the trustee shall observe the standards in dealing with the trust assets that would be observed by a prudent trustee dealing with the property of another. If the trustee has special skills, or is named trustee on the basis of representations of special skills or expertise, he is under a duty to use those skills.

Florida case law is likewise well settled regarding trustee duties and liabilities. Trustees must exercise due care, diligence, and skill in the administration of the trust. *Thomas v. Carlton*, 143 So. 780, 785 (Fla. 1932). Further, trustees are expected to "act in exacting good faith" while carrying out their duties in the administration of the trust. *Voorhies v. Blood*, 173 So. 705, 708 (Fla. 1937).

The parties who create a trust can and should include the trustees' standard of care and duties in the trust instrument. Section 737.302, *Florida Statutes*, expressly permits such drafting when it states "Except as otherwise provided by the trust instrument. . . ." In the instant case the Trustees' standard of care and performance was not delineated in the Trust Agreement. The Trust Agreement stated the purpose of the Trust as follows:

> Purpose: This Trust is organized for the primary purpose of liquidating the assets transferred to it with no objective to continue or engage in the conduct of a trade or business.

The initial burden is on the trust beneficiaries to prove that a breach of duty occurred which proximately caused the injury. *Ft. Myers Memorial Gardens v. Barnett Banks*, 474 So.2d 1215, 1218 (Fla. 2d DCA 1985). If that is established, the burden shifts to the trustee to demonstrate that the loss would have occurred in the absence of a breach. *Id.* at 1218. In the instant case, there is an exculpatory clause in the Trust Agreement limiting the Trustees' personal liability except for "proven dishonesty".

The Bankruptcy Court ruled that the appellants did not sustain their burden of proof to establish that McHale breached his duty. That ruling followed many months of evidentiary hearings in which the parties had ample opportunity to present extensive evidence and testimony. The Bankruptcy Court reached that determination in spite of sharp criticism about McHale's performance as Trustee of the Captran Creditors' Trust.

Rule 8013 of the bankruptcy rules, which this Court applies in this case, mandates the application of the "clearly erroneous" standard of review to the Bankruptcy Court's finding of fact. As stated by the United States Supreme Court:

> The trial judge's major role is the determination of fact, and with experience in fulfilling that role comes expertise. Duplication of the trial judge's efforts in the court of appeals would very likely contribute only negligibly to the accuracy of fact determination at a huge cost in diversion of judicial resources. In addition, the parties to a case on appeal have already been forced to concentrate their energies and resources on persuading the trial judge that their account of the fact is the correct one; requiring them to persuade three more judges at the appellate level is requiring too much.

Anderson v. City of Bessemer, 470 U.S. 564, 574-75, 105 S.Ct. 1504, 1512, 84 L.Ed.2d 518, 529 (1985). *See also*,

Richmond Leasing Co. v. Capital Bank, N.A., 762 F.2d 1303 (1985).

Finding the Court's reasoning in *Anderson* equally applicable to this case, this Court finds nothing clearly erroneous about the Bankruptcy Court's conclusion that McHale did not breach his duty as Trustee of the Captran Creditors' Trust. The lower Court's conclusion is well supported by the fact that the CCT was not an ordinary Trust. Moreover, McHale had an unenviable task of administering a Trust in which the parties actively participated while protecting competing interests.

The next issue for discussion is the exculpatory clause in the Trust Agreement. This court reviews that issue without conceding that a breach occurred to invoke that provision of the Trust Agreement. Technically, any consideration of the exculpatory clause is moot until appellants prove that a predicate breach occurred resulting in injury.

In the instant case, the Trust Agreement has an exculpatory clause pertaining to Trustee liability. The actual provision states as follows:

> Trustee Liability. Except for proven dishonesty, a Trustee shall not be personally liable for any act or omission in connection with his duties as Trustee.

There is no recital in the Trust Agreement defining what the parties meant by dishonsty. The Trust Agreement was the product of extensive negotiations, it was freely negotiated, and the parties were represented. In addition, Massari, appellants' attorney, was instrumental in drafting the Trust Agreement.

Appellants contend that the exculpatory clause in the Trust Agreement is against public policy and repugnant to the law. Moreover, appellants argue that public policy dictates that, at most, the exculpation provision only immunized appellees from liability for good faith errors in judgment.

Exculpatory clauses as a general rule are neither for or against public policy. Each exculpatory clause deserves independent review based on many considerations. Foremost in any review is the language of the exculpatory clause and whether it applies to the instant case. Other factors include, but are not limited to: how the exculpatory clause limits liability, intent of the parties, and the manner in which the exculpatory clause was made a part of the agreement.

The Bankruptcy Court accurately summarized the law concerning exculpatory clauses. The Courts have upheld exclupatory provisions in trust agreements. *Morrissey v. Curran*, 483 F.2d 480 (2d Cir. 1973), *cert. denied*, 414 U.S. 1128 (1974). *See also, Kolentus v. Avco Corp.*, 798 F.2d 949 (7th Cir. 1986), *cert. denied*, 479 U.S. 1032 (1987). Generally, exculpatory clauses are construed according to their plain meaning against the trustee. *Knauer v. Barnett*, 360 So 2d 398, 405 (Fla. 1978). Exculpatory clauses will not save a trustee from liability for certain breaches deemed especially reprehensible, for example, willful and intentional breaches, acts of bad faith, dishonesty, acts of gross negligence, and the like. G. Bogert, *Trusts*, 94 (6th ed. 1988).

No Florida cases are cited to define exactly what dishonesty means as it pertains to trustees. Appellants cite *Miami National Bank v. Pennsylvania Insurance Co.*, 314 F. Supp. 858, 868 (S.D. Fla. 1970), for the proposition that "dishonest" conduct is a reckless disregard for the beneficiaries' interests. Appellants also cite *Brandon v. Holman*, 41 F.2d 586, 588 (4th Cir. 1930) as authority that "dishonesty can be committed by passive permission, or failure to prevent, or helping by not hindering when it is one's duty to prevent or by negligence or by voluntary oversight." The *Brandon* court ruled that "*connivance with others* (emphasis added) may be committed by passive permission, or failure to prevent, or helping by not hindering when it is one's duty to prevent, or by negligence or voluntary oversight." *Id.* at 588. Later in

the *Brandon* decision, connivance was defined as "an agreement or consent, indirectly given, that something unlawful shall be done by another." *Id.* at 588. In *Glen Falls Indem. Co. v. National Floor & Supply Co.*, 239 F.2d 412, 413 (5th Cir. 1965) the Fifth Circuit stated that "for an act to be 'dishonest' within the meaning of a fidelity suretyship bond, there must exist the element of moral turpitude or want of integrity."

The Bankruptcy Court upheld the exculpatory clause in the Trust Agreement. This Court concludes that as a matter of law, the Bankruptcy Court did not err in upholding the exculpatory clause in the Trust Agreement. The exculpatory clause in the instant case was part of a Trust Agreement produced through extensive negotiations. The parties were in equal bargaining positions, knowledgeable and represented by counsel. Further, appellants' attorney was instrumental in drafting the Trust agreement. This Court finds no reason to conclude that the exculpatory clause in the instant case is against public policy or repugnant to the law of Florida.

As a related matter, this Court finds nothing "clearly erroneous" about the Bankruptcy Court conclusion that McHale was not a dishonest Trustee.

II. THE BANKRUPTCY JUDGE DID NOT ERR BY WITHHOLDING A FINAL DEFAULT JUDGMENT AGAINST McCONNELL EVEN THOUGH A DEFAULT WAS ENTERED AGAINST HIM.

Defaults in adversary proceedings are governed by Rule 55, Fed. R. Civ. P. *See* Bankruptcy Rule 7055.

Fed. R. Civ. P. 55 provides:

> Rule 55. Default
>
> (a) Entry. When a party against whom a judgment for affirmatvie relief is sought has failed to plead or otherwise defend as provided by the rules and that

> fact is made to appear by affidavit or otherwise, the clerk shall enter the party's default.
>
> (c) Setting Aside Default. For good cause shown the court may set aside an entry of default. . . .

Appellee and co-Trustee McConnell failed to timely file an answer to appellants' initial Complaint. A default was entered against him by the Clerk before trial commenced in the Bankruptcy Court. Appellants filed an Amended Complaint after the Clerk's default was entered against McConnell. Appellee McConnell did not attend the trial that was held in the Bankruptcy Court.

The Bankruptcy Court did not enter a Final Judgment against McConnell. It held that appellants presented no meaningful evidence concerning McConnell's conduct as co-Trustee. In light of that, the Bankruptcy Court decided it was inappropriate to enter a judgment against McConnell.

This Court holds as a matter of law that Judge Paskay correctly exercised his discretion in not entering final judgment against appellee McConnell. The disposition of a motion for entry of a default judgment lies within the court's sound discretion. *Mason & Hanger-Silas Mason Co. v. Metal Trades Council*, 726 F.2d 166 (5th Cir. 1984). Generally, the Court considers a variety of factors when exercising its discretion for entry of a default judgment. This Court favors decisions on the merits and finds no reason to conclude that Judge Paskay abused his discretion in withholding final judgment against appellee McConnell.

III. McHALE, AND McHALE, EZZELL & CO., P.A. DID NOT BREACH THEIR CPA DUTY OF CARE TO APPELLANTS.

Section 737.302, *Florida Statutes*, states in part:

> . . . If a trustee has special skills, or is named trustee on the basis of representations of special skills or expertise, he is under a duty to use those skills.

The parties and the Bankruptcy Court do not disagree that Section 737.302 applies to the Trustees of the Captran Creditors' Trust. However, the parties disagree on whether McHale used his CPA skills while a Trustee and whether his CPA firm is includable in this action because McHale acted as a Trustee.

Based on expert testimony, the Bankruptcy Court concluded, that McHale did not fall below the standards of a CPA. Given that conclusion, it follows that McHale's CPA firm is not liable.

There are no Florida decisions concerning trustees with special skills or trustees duty to use special skills under Section 737.302, *Florida Statutes*. Based on the plain meaning of the statute, this Court concurs that McHale had a duty to use his CPA skills while he was a Trustee of the Trust.

This Court defers to Judge Paskay as the trier of fact on the evidentiary issues of this case. As noted earlier, Rule 8013 of the bankruptcy rules, mandates the application of a "clearly erroneous" standard of review to the Bankruptcy Court's findings of fact. This Court finds nothing clearly erroneous about the Bankruptcy Court's conclusion concerning whether McHale used his CPA skills. Judge Paskay heard expert testimony from both sides and concluded that appellants did not sustain their burden of proof.

CONCLUSION

This Court, having carefully considered the issues on appeal, and based on the foregoing, concludes that the Bankruptcy Court did not err in its decision denying Appellants' claims. Accordingly, it is

ORDERED that the Bankruptcy Court's Final Judgement entered on April 17, 1990 is AFFIRMED. The Clerk of this Court is directed to enter judgement for Appellees in accordance with this Order, and dismiss the case.

DONE and ORDERED in Chambers, in Tampa, Florida, on this the 14th day of June, 1991.

/s/ Elizabeth A. Kovachevich
ELIZABETH A. KOVACHEVICH
United States District Judge

Copies to:

All parties and counsel of record

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE MIDDLE DISTRICT OF FLORIDA
TAMPA DIVISION

Case No. 85-0045-8P1

IN RE: CAPTRAN CREDITORS' TRUST,
Debtor

Adv. No. 87-158

CAPTRAN CREDITORS' TRUST, CLUB BAHA, LTD., a foreign corporation and TROPICAL PROPERTIES, LTD., a foreign corporation,
Plaintiff

v.

DAVID MCCONNELL, GERALD MCHALE, and MCHALE, EZZELL AND CO., a Florida professional association,
Defendants

FINDINGS OF FACT, CONCLUSIONS OF LAW AND MEMORANDUM OPINION

THIS is a confirmed Chapter 11 case, and the matter under consideration is a three-count Complaint by Captran Creditors Trust (CCT), Club Baha, Ltd. (Club Baha), and Tropical Properties, Ltd. (Tropical Properties) against David McConnell (McConnell), Gerald McHale (McHale), and McHale, Ezzell and Co., P.A. The Plaintiffs seek both compensatory and punitive damages in Count I based on the alleged breach of fiduciary duty owed to the Plaintiffs by Defendants McConnell and

McHale. The Plaintiffs in Count II seek compensatory and punitive damages for the alleged professional negligence of Defendants McConnell and McHale. In Count III, the Plaintiffs seek damages and other relief from Defendants McConnell, McHale, and McHale, Ezzell, and Co. for their alleged violations of § 772 of the Florida Statutes.

Although Defendant McConnell failed to timely file an answer to the Plaintiffs' Complaint and a default was entered against him by the Clerk before this trial commenced, a final judgment was not entered against McConnell. Additionally, Count III of the Plaintiffs' Complaint was dismissed by Order of this Court after the conclusion of the evidence presented at the final evidentiary hearing. This leaves for consideration the claims set forth in Counts I and II of the Complaint, that is whether McHale is liable for damages based on a breach of fiduciary duty and based on alleged negligence of a professional.

This Court, having heard extensive testimony of witnesses and having considered the documentary evidence, together with the record, now finds and concludes as follows:

In 1982, Captran Resorts International, Inc. (CRI), a corporation based in Lee County, Florida, was engaged in the business of developing resorts and selling timeshare interests to the public. At the same time, CRI through its president, Keith Trowbridge, entered into a joint venture with Club Baha and Tropical Properties, which were controlled by Jack Grabowski, for the development of a similar enterprise in the Bahamas. A disagreement between the parties resulted in litigation which ultimately concluded with a $1.7 million Final Judgment against CRI and its president, Trowbridge, and in favor of Club Baha and Tropical Properties. (Plaintiffs' Exh. No. 1.)

CRI, faced with the inability of satisfying the judgment and the possibility of losing some, if not all, of its

property because it could not post a supersedeas bond, filed a voluntary Petition for Relief under Chapter 11 of the Bankruptcy Code in this court on July 16, 1982. Soon after CRI filed its bankruptcy petition, CRI and some of its largest creditors, including Club Baha and Tropical Properties, entered into extensive negotiations. The purpose of their negotiations was to ultimately satisfy CRI's creditors and to resolve CRI's problems outside of the provisions of Chapter 11 and the bankruptcy court. (Plaintiffs' Exh. No. 1.)

The negotiations resulted in an agreement which provided that the creditors of CRI would form a trust, Captran Creditors Trust (CCT). The assets of CRI, with one minor exception, were to be transferred to CCT to be the Trust res, and the creditors of CRI were to be the Trust beneficiaries. The Defendants McConnell, an attorney, and McHale, a certified professional accountant (CPA), were appointed as the initial Trustees for this newly created Trust. A copy of the Agreement, a synopsis of its development, and copies of related documents are included in what is referred to as "the yellow book." (Plaintiffs' Exh. No. 2.) The Agreement was finalized in December, 1982. Based on the settlement, this Court entered an Order granting CRI's Motion to Dismiss the Chapter 11 case of CRI on December 6, 1982.

The Agreement provided that CCT would acquire from CRI certain specified assets of CRI and would assume any debts and liabilities associated with those assets. The assets transferred to CCT would be marketed and sold, and the net proceeds of the sales would go to the Trust for the benefit of the Trust beneficiaries. Under the Agreement, CRI was to act as the marketing agent for the Trust properties and, as a condition of the Agreement, was to receive 38% of the sale price of the properties sold.

CRI did, in fact, act as the marketing agent for the Trust properties. All sales were through a real estate

firm owned and controlled by Trowbridge, and they were processed through Northern American Title Insurance Agency, Inc. (NATIA), a title company also owned and controlled by Trowbridge. All sales records of the Trust properties were under the exclusive control of CRI's controller, George Mills (Mills), and there is no doubt that McHale acepted the recordkeeping of Mills without question or without any independent verification. NATIA handled all closings and maintained all of the records regarding the sales of timeshares. Evidence produced at trial leaves no doubt that neither McHale nor McConnell kept any records regarding the sales transactions; instead, they simply let Trowbridge and NATIA handle all of the details regarding the sales and recordkeeping of CRI.

The Agreement specifically described the Trustees' duties, powers, and liabilities. Regarding the Trustees' liability, the Agreement provided that "except for *proven dishonesty*, a Trustee shall not be personally liable for any act or omission in connection with his duties as Trustee." (Plaintiffs' Exh. No. 1 at p. 117.) (emphasis supplied) The Agreement further provided that the Trust was created "for the primary purpose of liquidating the assets transferred to it with no objective to continue or engage in the conduct in any trade or business."

Notwithstanding the stated purpose of the Trust, i.e., to liquidate the Trust assets, the evidence presented clearly established that CRI continued to develop and build on two of the undeveloped properties conveyed to the Trust by the Agreement. The record leaves no doubt that the Trustees agreed, at least tacitly, to this activity by CRI, and at no time voiced any objection to it. On the contrary, McHale consented to this development because he believed it would maximize the return to the beneficiaries of the Trust. It appears that even though the Trust Agreement did not authorize any additional development, this development produced a net benefit to the

Trust to the extent of $1.7 million. (Defendant's Exh. No. 7.)

It further appears that both the Trustees and Grabowski attempted to sell all of the Trust assets in bulk, but were unable to find a buyer. (Defendant's Exhs. No. 51, No. 52.) To solve their dilemma, the Trustees developed a liquidation plan pursuant to which the Trust assets would be distributed in-kind to the beneficiaries of the Trust in exchange for extinguishing their beneficiary interest in the Trust. (Plaintiffs' Exh. No. 66.) However, CRI resisted in-kind distribution (Defendant's Exh. No. 6), and threatened to sue the Trustees if they proceeded with this plan. (Defendant's Exh. No. 6.) This resistance by CRI is understandable in light of a provision in the Agreement which preserved for CRI any residual interest in the Trust properties, if one remained after the liquidation of the Trust assets and after the satisfaction of the interest of the Trust beneficiaries.

In order to protect their position, the Trustees filed a suit for declaratory relief requesting that the Circuit Court of Lee County, Florida approve the in-kind distribution. The Trustees also sought a temporary restraining order to remove CRI as the marketing agent for the Trust assets; however, that request was denied. (Defendant's Exhs. No. 44 and No. 47.) While this in-kind distribution was clearly contemplated by the Agreement, it was never consummated. Be that as it may, this Court is satisfied that the Trustees did nothing improper by promulgating this plan, and certainly they were not negligent for trying to effectuate this type of distribution. (Plaintiffs' Exh. No. 1.)

During the pendency of the declaratory suit in the Circuit Court of Lee County, several of the Trust beneficiaries assigned their interest in the Trust to Club Baha. As a result, Club Baha ended up with over 90% of the beneficial interests of the Trust. Soon after the assignments were made, Grabowski, as president of Club

Baha and Tropical Properties Ltd. and on behalf of 90% of the Trust beneficiaries, discharged McHale and McConnell from their duties as Trustees and appointed successor Trustees. (Plaintiffs' Exh. No. 44.) McHale submitted as his final accounting of his Trusteeship a report prepared by Mills (Plaintiffs' Exh. No. 2). By all accounts, this report did not even come close to being an acceptable final accounting of a trustee, and it did not pretend to be one. The report was nothing more than a compilation of the Trust assets and the beneficiary interests that existed at the time the Trust was created; it did not reflect what really existed when McHale's Trusteeship ended.

The successor Trustees and Club Baha then entered into an agreement pursuant to which the successor Trustees agreed to convey the bulk of the Trust assets to Club Baha, in exchange for Club Baha's interest in the Trust. Before the transfer of the Trust assets by the successor Trustees to Club Baha was finalized, certain parties who claimed to be creditors of CCT filed an involuntary Petition against CCT in this Court. After extensive preliminary skirmishes and prior to the trial, CCT finally consented to the entry of the order for relief on the eve of the trial. The Plan of Reorganization proposed by Club Baha and Grabowski, which was a total liquidation plan, was ultimately confirmed. This Plan of Reorganization basically produced the very same result that was contemplated by the in-kind distribution plan proposed by the original Trustees, McHale and McConnell.

Based on the foregoing facts, the Plaintiffs filed a three-count Amended Complaint against the Defendants. The Plaintiffs' claim in Count I is based on the contention that McHale, in his representative capacity as co-Trustee, breached his fiduciary duty to the Trust beneficiaries. In support of this proposition, the Plaintiffs contend that McHale owed a duty to discharge his obligation as Trustee in good faith and with ordinary care and dili-

gence. The Plaintiffs argue that McHale breached that duty, especially because he earlier served as an accountant for Club Baha and Tropical Properties before the Trust was even formed, and he therefore owed a special fiduciary duty to these Plaintiffs. The claim in Count II is based on the contention that McHale is liable for damages which the Plaintiffs allegedly incurred as a result of McHale's purported professional negligence as a CPA. As noted earlier, the claim in Count III was dismissed by this Court at the close of the evidence.

This record leaves no doubt that the conduct of McHale as a Trustee certainly left a lot to be desired, and that his detached, lackadaisical attitude toward the Trust affairs may be charitably characterized at most as benign neglect. McHale's lack of involvement with the trust was clearly evidenced by his unquestioned acceptance of the Mills Report as a final accounting of his Trusteeship. In addition, it is clear from the record that McHale granted almost a complete free reign to Trowbridge, Mills and NATIA involving sales of Trust assets, sales closings, and the recordkeeping of the Trust assets. It must be conceded that *Fla. Stat.* § 737.302 provides that a trustee with special skills is under a duty to use those skills. Thus, if McHale's performance is measured by the standard of a CPA who was engaged to serve in that capacity, one would be hard pressed to conclude that his performance met the standards of a reasonable CPA.

The Plaintiffs also argued that McHale should be held to a higher standard when his performance as Trustee is evaluated. Specifically, the Plaintiffs contended that because McHale represented the Plaintiffs Tropical Properties and Club Baha in connection with their 1982 litigation against CRI, he owed a special fiduciary duty to the Plaintiffs.

Considering the proposition urged by the Plaintiffs, this Court is satisfied that McHale was not engaged to serve as a CPA-Trustee. Further, McHale is not bound

by any special higher standard because the firm in which he is an accountant represented the Plaintiffs Tropical Properties and Club Baha in their litigation against CRI.

The Trust Agreement does not provide that McHale was to serve as a CPA for the benefit of the Trust. The yellow book does provide a brief history of McHale's background, and includes the fact that he was a partner in the accounting firm which represented the Plaintiffs Tropical Properties and Club Baha in their litigation against CRI. However, it is clearly stated in the yellow book that the biographical sketch and disclosure of the Trustee's business interest was made available because it might appear that there was a conflict of interest between the Trustee and CCT. (Plaintiffs' Exh. No. 1.) Alternatively, assuming without admitting, that if McHale is judged as a CPA Trustee, this Court is satisfied that the expert testimony presented at trial showed that McHale did not, in fact, fall below the standards of a CPA, and the Plaintiffs did not prove otherwise by clear and convincing evidence.

The exculpatory clause in the Trust Agreement specifically addresses the liability of a trustee in the exercise of his duties as a trustee. Thus, the ultimate question is whether or not the enforcement of this exculpatory clause would be contrary to public policy and should be disregarded, or whether this Court should give full effect to the unambiguous language of the Trust Agreement. There is no doubt that Grabowski was a highly sophisticated businessman, and the parties were of equal bargaining power. This was certainly an arm's length transaction. The Trust beneficiaries cannot argue that they were either ill-represented or unsophisticated. This Court is satisfied that it is appropriate to enforce this exculpatory clause.

Considering the exculpatory clause, it should be noted that several courts have upheld exculpatory provisions in trust agreements. An exculpatory clause in a trust agree-

ment which provided that the trustees shall not be liable for the making of any investments, nor for any loss or diminution of the trust fund "except due to their own willful misconduct" was upheld in *Morrissey v. Curran*, 483 F.2d 480 (2d Cir. 1973). A similar provision was used to exonerate a trustee bank of liability, notwithstanding the Plaintiff's argument that the provision served to excuse the trustee from exercising reasonable care in managing the Plaintiff's pension assets. *Kolentus v. Avco Corp.*, 798 F.2d 949 (7th Cir. 1986).

This Court recognizes that although a Trustee's liability may be limited in a Trust, such a limiting provision will be strictly construed against the Trustee and will not save the Trustee from liability for bad faith. 56 *Fla. Jur 2d* § 47. It is equally axiomatic, however, that a Trust provision will be construed according to its plain meaning where the words are not uncertain or ambiguous. 56 *Fla. Jur. 2d* § 5, 76 *Am. Jur. 2d* § 19, *Knauer v. Barnett*, 360 So. 2d 398, 405 (Fla. 1978). Based on the evidence presented at trial, this Court is satisfied that although McHale might have acted in a less than professional manner and may possibly have acted beneath the standard of sound business practices, he was not dishonest. In fact, there is not one scintilla of evidence in this record which would support a claim that he acted in a dishonest fashion while dealing with the Trust assets. There were neither allegations nor evidence that McHale engaged in self-dealing, or that he profited from his actions as a co-Trustee. This Court is therefore satisfied that absent any showing of dishonesty on his part, he cannot be held personally liable for any acts or omissions in the performance of his duties as co-Trustee.

As noted earlier, the Clerk previously entered a default against Defendant McConnell, but no final judgment has been entered by default against McConnell. In light of the fact that there was no meaningful evidence presented by the Plaintiff concerning any conduct by McConnell, who is a co-Trustee, this Court is satisfied that it would

not be appropriate to enter a judgment against this Defendant in spite of the fact of the entry of the default.

A separate Final Judgment will be entered in accordance with the foregoing.

DATED at Tampa, Florida, on April 4, 1990.

/s/ Alexander L. Paskay
ALEXANDER L. PASKAY
Chief Bankruptcy Judge

CC: Attorney Plaintiff—Malka Isaak
Co-Counsel—Richard W. Epstein
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Charles W. Pittman

Supreme Court, U.S.
FILED
MAR 5 1993
OFFICE OF THE CLERK

No. 92-1332

IN THE

Supreme Court of the United States

OCTOBER TERM 1992

CAPTRAN CREDITORS TRUST, CLUB BAHA, LTD. and TROPICAL PROPERTIES, LTD.,
Petitioners,

v.

DAVID W. McCONNELL, GERARD A. McHALE JR. and McHALE, EZZELL & CO., P.A.,
Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

BRIEF IN OPPOSITION FOR RESPONDENTS, GERARD A. McHALE JR., and McHALE, EZZELL & CO. P.A.

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I

QUESTIONS PRESENTED

IS ANY BASIS FOR THE EXERCISE OF THIS COURT'S DISCRETIONARY CERTIORARI JURISDICTION PRESENTED BY THIS CASE WHERE: (1) THE TRUST AGREEMENT'S LIMITATION OF TRUSTEE LIABILITY IS GOVERNED BY FLORIDA AND NOT FEDERAL LAW OR POLICY; (2) THE CIRCUIT COURT AFFIRMED, WITHOUT OPINION, THE BANKRUPTCY AND DISTRICT COURTS' DETERMINATION THAT THERE WAS NO ACTIONABLE BREACH OF ANY DUTY UNDER ANY STANDARD, THUS MOOTING THE APPLICABILITY OF THE LIMITATION OF LIABILITY CLAUSE, AND (3) THE CLAUSE IS VALID IN ANY EVENT?

PARTIES TO THE PROCEEDING

All parties in the Court below are listed in the caption of the cause in this Court. Respondent, McHale, Ezzell & Co., P.A., is a professional corporation having no parent or subsidiaries within the meaning of the Supreme Court Rule 29.1. Petitioner, Club Baha, Ltd., is a wholly owned subsidiary of Petitioner, Tropical Properties, Ltd.

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Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

BRIEF IN OPPOSITION FOR RESPONDENTS, GERALD A. McHALE, JR., and McHALE, EZZELL & CO. P.A.

STATEMENT OF THE CASE

Course of Proceedings Below

This cause began as an adversary proceeding in the reorganization of Captran Creditors' Trust, Debtor (CCT) in the Bankruptcy Court of the Middle District of Florida, on a three count Complaint by Petitioners, CCT, Club Baha, Ltd., (Club Baha) and Tropical Properties, Ltd. (Tropical) against David McConnell (McConnell) and these Respondents, Gerald McHale (McHale) and McHale, Ezzell & Co., P.A. (the P.A.). (A. 2a, 20a).[1]

1 (A.) shall refer to the appendix to the Petition.

Count I was based upon allegations of breach of fiduciary duty owed to Petitioners by McConnell and McHale. Count II alleged professional negligence against McHale and McConnell. Count III sought relief under §722, Florida Statutes (1985), against McConnell, McHale and the P.A. (A. 20a-21a). Count III was dismissed by the Bankruptcy Court after trial. (A. 2 la). That dismissal is not implicated in any way in the question sought to be posed by Petitioners.

Although a default was entered against McConnell for failure to timely file an answer in the Bankruptcy Court, a Final Judgment was not entered against McConnell because " . . . there was no meaningful evidence presented by the Plaintiff concerning any conduct by McConnell who is a Co-Trustee . . .". (A. 28). That judicial action is not implicated in the question sought to be posed by the Petitioners.

The Bankruptcy Court entered its findings Of fact, conclusions of law and memorandum opinion in favor of McHale and the P.A. on April 4, 1990. (A. 20a and 29a).

Petitioners' appealed to the United States District Court for the Middle District of Florida, which affirmed the judgment below on June 17, 1991. (A. 2a). In affirming, the District Court used the standard of appellate review which requires that the findings of fact of the Bankruptcy Court are not to be set aside unless clearly erroneous. Bankr. R. 8013; *Anderson v. City of Bessemer*, 470 U.S. 564, 574-575, 84 L.Ed 2d 518, 519 105 S.Ct. 1504, 1512 (1985). However, the District Court applied an independent *de novo* review of all conclusions of law and the legal significance to be accorded to the facts. *E.g., In re: Owen*, 86 B.R. 691, (M.D. Fla. 1988). (A. 3a).[2]

Respondents then appealed to the United States Court of Appeals for the Eleventh Circuit. On November 10, 1992, the

2. Aff'd 877 F.2d 44 (llth Cir. 1989), rev'd, other grounds *Owen v. Owen*, __U.S.__, 114 L.Ed 2d 350, 111 S. Ct. 1833 (1991).

Circuit Court affirmed the District Court without a written opinion under Eleventh Circuit Rule 36-1. (A. la)[3]

STATEMENT OF THE FACTS

Preliminary Statement

Petitioners avoid the facts as found by the District Court and affirmed by the Eleventh Circuit. Instead, Petitioners sponsor an incomplete, erroneous and selective combing of the evidence presented in the Bankruptcy Court and the findings of both the Bankruptcy and District Courts. Instead of the District Court's opinion as affirmed by the Eleventh Circuit, which is the focal point of certiorari jurisdiction, Petitioners attempt to rely upon rhetoric and unsupported contentions. (A. la 2a-19a).

Respondents are mindful of the admonishment of Supreme Court Rule 15.1. However, to confront all of the misstatements and contentions advanced by the Petition, which were rejected below, would render this Brief in Opposition far too lengthy. The facts as found by the District Court and affirmed by the Eleventh Circuit come to this Court with a presumption of correctness. Because a Brief in Opposition is not a brief on the "merits," this Court's initial inquiry is focused upon facts and law " . . . which have a bearing on the question of what issues would properly be before the Court if certiorari were granted." S.Ct. R. 15.1. Respondent's Statement of the Facts will be directed toward that consideration, as well as Supreme Court Rule 10.1.

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3. 11th Cir. R. 36-1, as applicable to this case, provides:

> When the court determines that any of the following circumstances exist:
>
> (a) judgment of the district court is based on findings of fact that are not clearly erroneous;
>
> ***
>
> (e) judgment has been entered without an error of law;
>
> and an opinion would have no precedential value, judgment or order may be affirmed or enforced without opinion.

The Facts

Contrary to the implications of the Petition, and the artful phrasing of the Question Presented in the Petition, this case does not concern " . . . Federal public policy for Trustees in a federal bankruptcy proceeding . . . ". CCT was a Trust organized under the laws of the State of Florida. Respondents never functioned as Trustees under the supervision of any bankruptcy court or any federal court.

CCT was organized to use assets of Captran Resorts International, Inc. (CRI) to satisfy creditors of CRI outside of the jurisdiction of the Bankruptcy Court. The major creditor of CRI, and CCT was Club Baha (controlled by Jack Grobowsky). (A. 3a -4a).

Contrary to the implication at page 3 of the Petition, McHale was not the primary negotiator of the agreement for Club Baha. As found by the District Court on uncontested facts, the " . . . major author . . . " and the ". . . chief author of the legal structure of the Trust . . ." was Attorney Massari, who represented Grobowsky and Club Baha. (A. 4a). The District Court and the Bankruptcy Court specifically noted that the Trust Agreement was the product of extensive negotiations between parties of equal bargaining power. (A. 7a, 14a, 16a). As stated by the Bankruptcy Court (A. 27a):

> There is no doubt that Grobowsky was a highly sophisticated businessman, and the parties were of equal bargaining power. This was certainly an arms' length transaction. The Trust beneficiaries cannot argue that they were either ill-represented or unsophisticated.

CRI's Chapter 11 case was dismissed December 6, 1982 following finalization of the Trust Agreement. (A. 4a). The stated purpose of CCT was:

> . . . liquidating the assets transferred to it with no objective to continue or engage in the conduct of a trade or business. (A. 6a).

The Trust Agreement also limited the Trustee's liability:

> Except for proven dishonesty, a Trustee shall not be personally liable for any act or omission in connection with his duties as Trustee. (A. 7a).

McHale and McConnell were appointed Trustees. It was considered that McHale was aligned with Club Baha and Grobowsky, and McConnell was aligned with CRI. (A. 5a).

The Trust was not liquid at the time of its inception. It consisted of CRI's assets, and liabilities connected with those assets. The assets were mainly 1400 time share unit weeks at 5 resort properties, land which had not been developed, two mortgage portfolios and a promissory note. Although the beneficiaries were CRI's creditors, CRI retained a residual interest in the CCT properties if any remained after liquidation and satisfaction of the interests of the Trust beneficiaries. (A. 5a).

The land in Sanibel Island Beach Club (SIBC) was a major asset of CCT.[4] SIBC was designed as a multiple building development to be built in phases. (A. 5a). One building was almost completed but had not been granted a certificate of occupancy (Bldg. 10) . Permits for two more buildings had been issued (Bldgs. 8 and 9). Sanibel Island enforces a Rate Growth Ordinance (ROGO) which affects the time and extent of development which is allowed. The land for SIBC Buildings 5, 6 and 7 was an assert of the Trust, but building permits had not been issued. Although the Trust owned the land, CRI (the original debtor) owned the development rights to all SIBC land. The undisputed evidence showed that CRI would not have put the land comprising SIBC 5, 6, 8 and 9 into the Trust if it had not expected a return of a residual interest in the Trust at termination after payment of creditors. The Lee County, Florida Building Department had previously approved the actual construction of Buildings 8 and 9 and the building permits would

4. It was due to the efforts of McHale prior to accepting appointment as a Trustee that this asset was included in the trust assets.

have been lost if the development had not proceeded. (A. 5a).

The assets of the Trust were to be marketed and sold for the beneficiaries of the Trust. The Trust specifically called for CRI to receive 38 percent marketing fee based upon the sale price of the property and allowed for the CCT properties to be sold at 10 percent discount. Any other discounts were deducted from CRI's marketing fee. The Trust always received 62 percent of the net sale proceeds. Actual sales of CCT properties were handled by a real estate title agent controlled by Trowbridge, North American Title Insurance Agency, Inc. (NATIA) (A. 6a).

Contrary to the Petition's attempted implication at p. 3, McHale was not engaged as a CPA by Club Baha during his tenure as Co-Trustee, neither was the P.A. in any way a Co-Trustee. There was no engagement letter, there was no agreement to act as a CPA for Club Baha, and the expert testimony credited by the District Court and the Bankruptcy Court was that the actions of McHale did not amount to acting as a CPA. (A. 17a-18a, 26a-27a).

In 1983 CRI continued to develop Buildings 8 and 9 at SIBC with the consent of McHale who believed that it would maximize return to the Trust beneficiaries. Although the Trust Agreement did not authorize any such additional development, far from hurting the Trust, this continued development resulted in a net benefit to the Trust of $1.7 million dollars. (A. 7a).

In 1983, both of the Trustees and Grobowsky attempted to sell the assets of the Trust in bulk, but they could not find a buyer. The Trustees then attempted a distribution of the Trust assets in kind. This distribution was resisted by CRI because of its residual interest in the Trust assets after creditors were paid. CRI threatened litigation, and the Trustees filed a state court action for declaratory relief requesting court approval of a distribution in kind and a temporary restraining Order in an effort to remove CRI as marketing agent for Trust assets. (A. 7a, 24a). However, Grobowsky withdrew his support for the action shortly after it was begun and an order denying the restraining Order was entered by the Circuit

Court on March 8, 1984.[5]

During the pendency of the state court action, several beneficiaries of CCT assigned their beneficial interest to Club Baha, which then held over 90 percent of the creditors' claims under the Trust. Grobowsky then discharged McHale and McConnell as Trustees and appointed successor Trustees. These hand-picked Trustees then reached an agreement to transfer the bulk of CCT's assets to Club Baha in exchange for Club Baha's interest in the Trust. (A. 8a).

The transfer to Club Baha was interrupted by an involuntary petition in bankruptcy filed against CCT by parties claiming to be creditors. After the Bankruptcy Court ruled that CCT was a business Trust which could file for bankruptcy (*In re: Captran Creditors' Trust*, 53 B.R. 741 (M.D. Fla. 1985)), CCT consented to conversion to a voluntary Chapter 11. Following this conversion, Club Baha and Grobowsky proposed a plan of total liquidation which was confirmed. This plan resulted in an in-kind distribution of the CCT assets to the beneficiaries, which distribution was very similar to the one originally planned by McConnell and McHale. (A. 8a-9a).

At page 4, the Petition attempts to paint a picture of McHale accepting records without question from CRI's comptroller, Mills. Although the Bankruptcy Court stated that McHale granted " . . . almost a complete free reign to Trowbridge, Mills and NATIA involving sales of Trust assets, sales closing, and record keeping of the Trust assets . . . . " (A. 26a), this statement does not equate to accepting record keeping without question or verification. Although the records were kept by Mills of CRI, the trial testimony was that McHale required much extra documentation, and that he would not sign deeds on timeshare sales without being satisfied that the records were complete. This is reflected in the District Court's findings:

5. The evidence shows that Club Baha would have received the beginning of substantial pay-outs from the closings in SIBC 8 and 9. However, these closings were prevented by Grobowsky's refusal to release Club Baha's judgment lien in the state court action.

> The Trustees received weekly sales reports of Trust inventory, monthly schedules of closed sales, monthly balances in escrow, cumulative showings of use of escrow funds for development and construction purposes, escrow draw approvals and draw requests from the construction company. In addition, the Trustees met approximately bi-weekly with Mills. (A. 6a).

Pages 4-7 of the Petition constitute only contentions by the Petitioners concerning alleged defaults by McHale, and out-of-context quotations from the Bankruptcy Court's Order, to the exclusion of the District Court's findings and Order, which was affirmed by to the Eleventh Circuit.

There was absolutely no link between any of the alleged actions by McHale and any alleged damages to the Trust. Not only were the claimed damages refuted by the Respondent's, Petitioners called no appraisers or other witnesses to establish the Trust's value before and after the original Trustees were terminated. Petitioners could not even show that any meaningful rescission of time share sales occurred as a result of Trustee actions. (A. 9a). As recognized by the District Court, no actions by McHale resulted in any harm to the Petitioners:

> The Bankruptcy Court ruled that the appellants did not sustain their burden of proof to establish that McHale breached his duty. That ruling followed many months of evidentiary hearings in which the parties had ample opportunity to present extensive evidence and testimony. The Bankruptcy Court reached that determination in spite of sharp criticism about McHale's performance as Trustee of the Captran Creditors' Trust. (A. 13a).

Footnote 3 at page 5 of the Petition is but one example of Petitioners' distortion of the facts in this case. There was no "fire sale" of assets, as reflected by the lack of any such findings in either the Bankruptcy Court Order or the District Court Order. The facts show that the loan portfolio at issue was actually sold for a

much larger amount of mortgages receivable. The portfolio was rapidly decreasing in value because time share buyers would quit paying on the mortgage. The Trust was to replace the paper with substitute paper to maintain their collateral reserve. This loan portfolio would only have come back to the Trust if all of the mortgages had paid completely out at the end of the mortgage period.

At its inception, the Trust had zero liquidity. But at the time McHale was terminated, CCT had $1,824 in cash, $346,268 in escrow awaiting the release of Grobowsky's lien to close, which he refused to do, and $972,089 in mortgage notes receivable also awaiting release of Grobowsky's lien to close, which he refused to do.

The Trust Agreement provided for Club Baha to receive 62 percent of net proceeds after reserving funds for administration expenses and after payment of the first and second tier of creditors under the Trust Agreements. At the time Grobowsky prevented the closing, tier one and two of beneficiaries had been paid, and the Trustees were ready to pay the third tier which included Club Baha. The net result of the obstructive tactics used by Grobowsky was to take control of the $1.3 million dollar Trust and, through hand picked successor Trustees, to completely cut out CRI from its residual rights under the Trust.

The most disingenuous aspect of the Petition is its distorted portrayal of the District Court's ultimate determination as affirmed by the Eleventh Circuit. Petition, p. 8. Neither the District Court nor the Eleventh Circuit were under any "misunderstanding." The District Court's conclusions of law came after ". . . an independent *de novo* review of all conclusions of law and the legal significance accorded to the facts." (A. 3a).

Although the Bankruptcy Court did criticize certain aspects of McHale's performance as Trustee, it clearly rejected the Petitioners' claim that McHale breached any duty, much less *any duty* as measured by the liability limitation clause of the Trust. (A. 25a-27a). It was Petitioners' contention throughout that McHale should be judged by a higher standard which incorporated his sta-

tus as a CPA. (A. 26a). The Bankruptcy Court clearly rejected any claim of breach of duty *even if* McHale were judged as a "CPA Trustee":

> Alternatively, assuming without admitting that if McHale is judged as a CPA Trustee, this Court is satisfied that the expert testimony presented at trial showed that McHale did not, in fact, fall below the standards of a CPA, and the Plaintiffs did not prove otherwise by clear and convincing evidence. (A. 27a).

Again, the District Court also unequivocally held that, as a matter of fact and law, McHale did not breach any duty which resulted in any proven damage to the Petitioners. (A. 13a).

With respect to the limitation of liability or "exculpatory" clause the District Court affirmed the Bankruptcy Court and upheld the clause although it was not required to address the clause in light of its primary decision, on *de novo* review of legal issues, that there was no breach of *any* duty. (A. 16a). Its holding that the limitation of liability provision of the Trust Agreement was valid constituted only an alternative ground that was essentially *dicta*:

> . . . this Court finds nothing clearly erroneous about the Bankruptcy Court's conclusion that McHale did not breach his duty as Trustee of the Captran Creditors' Trust. The lower Court's conclusion is well supported by the fact that the CCT was not an ordinary Trust. Moreover, McHale had an unenviable task of administering a Trust in which the parties actively participated while protecting competing interests. (A. 14a).
>
> The next issue for discussion is the exculpatory clause in the Trust Agreement. This court reviews that issue without conceding that a breach occurred to invoke that provision of the Trust Agreement. Technically, any consideration of the exculpatory clause is moot until appellants prove that a predicate breach occurred resulting in injury. (A. 14a).

SUMMARY OF ARGUMENT

I

The Trust at issue in this cause is governed by Florida substantive law. Accordingly, the attempt by the Petition in its Question Presented and throughout to present this matter as one involving federal law and policy is totally without merit. Accordingly, the decision sought to be reviewed presents no basis for the exercise of this Court's discretionary certiorari jurisdiction under Supreme Court Rule 10, or otherwise.

II

Any issue concerning the limitation of trustee liability clause in the Trust Agreement, as sought to be presented by the Question Presented in the Petition, is moot. The District Court, following *de novo* legal review of legal conclusions applied to the facts, unequivocally held that McHale, as Trustee, breached no duty whatsoever. This conclusion was affirmed by the Circuit Court. Manifestly, this Court is not a court of select errors designed to grant additional appellate review to disgruntled litigators.

III

Regardless of the fact that application of the limitation of liability clause is moot under the District Court findings, affirmed by the Court of Appeals, its alternative determination that the clause was valid is correct.

This was not a normal "trust," but an attempt by competing and often antagonistic interests to work out the debt problem of CRI *outside* the jurisdiction of the Bankruptcy Court. The Trust Agreement, including the limitation of liability clause, was the result of long negotiations between antagonistic parties of equal bargaining power. Similar types of exculpatory clauses have been upheld by courts.

REASONS WHY THE PETITION SHOULD BE DENIED

I
NO COGNIZABLE FEDERAL LEGAL OR POLICY ISSUES ARE PRESENTED BY THE DECISION BELOW.

Despite the Petition' s attempt to couch the Question Presented in terms of ". . . federal public policy for trustees in a federal bankruptcy proceeding, . . .", it is quite evident that neither the case as a whole or the decisions below present any cognizable federal issue or controversy for this Court's determination. This is true with respect to the considerations of Supreme Court Rule 10, and the purpose of discretionary certiorari review generally. CCT was a business trust established under and governed by the substantive law of Florida, including all issues related to the duty of Trustees, breach of that duty, and the validity of any limitation of liability clause contained in the Trust Agreement.

The fact that CCT was placed into bankruptcy under Chapter 11, and the issues surrounding Petitioners' claims were tried in the Bankruptcy Court, does not operate to convert issues controlled solely by state law to a case involving either federal law or federal policy. Resolution of such issues under state law has no bearing whatsoever upon the resolution of any similar issues with respect to bankruptcy trustees, or any other trustee subject to federal law.

The Petitioners' attempt to manufacture a federal policy within the narrow confines of this case in order to attempt a wholesale retrial of the merits of the case in this Court, is, in a word, spurious. The assertion at page 8 of the Petition (p. 8) that "[t]his case presents a serious question of federal public policy that goes to the very heart of bankruptcy law . . ." constitutes more than disingenuous argument, it is a deliberate misrepresentation.

II
THE LIMITATION OF LIABILITY CLAUSE IN THE TRUST AGREEMENT IS NOT AT ISSUE BECAUSE OF THE ABSENCE OF ANY BREACH OF DUTY UNDER ANY STANDARD.

In essence, Petitioners are simply seeking a total retrial of their claims and rhetoric which have been rejected by three courts. Even a cursory review of the contentions of the Petition, and the Orders of the Bankruptcy and District Court, discloses a litigious disagreement with factual findings which were affirmed by the Circuit Court which saw no basis for even writing an opinion.

Indeed, as noted by the District Court, in light of the fact that there was no competent evidence presented by Petitioners to establish any breach under any standard, ". . . any consideration of the exculpatory clause is moot." (A. 14a).

This factual finding, affirmed by the Circuit Court, comes to this Court with the presumption of correctness. In order to address the question presented by the Petition, this Court would have to engage in an independent fact finding review process and reach a contrary conclusion on the issue of breached duty *vel non*.

Another example of the Petition's attempt to treat this Court as a mere appellate court of errors, is its treatment of Respondent, McConnell, at the close of the Petition at p. 13. The Petition presents no facts concerning Trustee McConnell because, as aptly noted by the Bankruptcy Court, it presented no evidence concerning his execution of his duties. (A. 28a). As stated by the District Court (A. 17a):

> The Bankruptcy Court did not enter a Final Judgment against McConnell. It held that appellants presented no meaningful evidence concerning McConnell's conduct as co-Trustee. In light of that, the Bankruptcy Court decided it was inappropriate to enter a judgment against McConnell.

> JThis Court holds as a matter of law that Judge Paskay correctly exercised his discretion in not entering final judgment against appellee McConnell. The disposition of a motion for entry of a default judgment lies within the court's sound discretion. *Mason & Hanger-Silas Mason Co. v. Metal Trades Council*, 726 F.2d 166 (5th Cir. 1984). Generally, the Court considers a variety of factors when exercising its discretion for entry of a default judgment. This Court favors decisions on the merits and finds no reason to conclude that Judge Paskay abused his discretion in withholding final judgment against appellee McConnell.

In reality, the Petition presents mere assertions, obviously in hope that this Court will retry issues determined in the Bankruptcy Court, reviewed under proper standards by the District Court, and affirmed by the Circuit Court under circumstances where the Circuit Court felt that an opinion would have *no precedential value*. In ignoring the stated basis for the District Court's decision as affirmed by the Circuit Court, Petitioners lose sight of the fact that courts of appeal are not just way points on the road to this Court. This Court does not act as a mere appellate tribunal to review questions of fact of interest only to the parties themselves. *See, e.g., NLRB v. Hendricks City Royal Electric Membership Corp.* , 454 U.S. 170, 176 n. 8, 70 L.Ed 2d 323, 330 (n. 8), 102 S.Ct. 216 (1981); *United States v. Johnston*, 268 U.S. 220, 227, 69 L.Ed 925, 926, 45 S.Ct. 96 (1925):

> We do not grant a certiorari to review evidence and discuss specific facts.

The Petition is nothing more than a final exhortation by disgruntled litigants which serves only to further exhaust the time and resources of Respondents and this Court.

III
THE LIMITATION OF LIABILITY CLAUSE IS VALID IN ANY EVENT.

The limitation of liability clause is valid, notwithstanding the fact that application of the clause became moot because of the absence of credible proof of an actionable breach of duty under *any* standard. (A. lla-14a).

Both the Bankruptcy Court and the District Court correctly analyzed the factors to be considered in enforcing the clause under the particular facts of this trust arrangement and correctly applied the facts to the law:

> Exculpatory clauses as a general rule are neither for or against public policy. Each exculpatory clause deserves independent review based on many considerations. Foremost in any review is the language of the exculpatory clause and whether it applies to the instant case. Other factors include, but are not limited to: how the exculpatory clause limits liability, intent of the parties, and the manner in which the exculpatory clause was made a part of the agreement.
>
> The Bankruptcy Court accurately summarized the law concerning exculpatory clauses. The Courts have upheld exculpatory provisions in trust agreements. *Morrisey v. Curran*, 483 F.2d 480 (2nd Cir. 1973), cert. denied 414 U.S. 1128 (1974) *See also, Koelentus v. Avco*, 798 F.2d 949 (7th Cir. 1986), cert. denied 479 U.S. 1032 (1987). Generally, exculpatory clauses are construed according to their plain meaning against the trustee. *Knauer v. Barnett*, 360 So. 2d 398, 405 (Fla. 1978). Exculpatory clauses will not save a trustee from liability for certain breaches deemed especially reprehensible, for example, willful and intentional breaches, acts of bad faith, dishonesty, acts of gross negligence, and the like. G. Bogert, *Trusts*, 94 (6th ed. 1988). (A. 15a).

From the beginning, CCT was not a normal "trust." It was an attempt to resolve CRI's debts outside of bankruptcy. It involved an attempt to balance competing and often antagonistic interests represented by Grobowsky and Club Baha on the one hand and Trowbridge and CRI on the other. (A. 14a).

Of necessity, any analysis of the validity of the Trust Agreement's limitation of liability clause must include a strong emphasis on the following undeniable fact, as noted by the District Court:

> The exculpatory clause in the instant case was part of a Trust Agreement produced through extensive negotiations. The parties were in equal bargaining positions, knowledgeable and represented by counsel. Further, appellant's attorney was instrumental in drafting the Trust agreement. (A. 16a).

Again, given the validity of the Trust Agreement, in order to reverse the Circuit Court, this Court would have to act as a superior court of select errors and review the voluminous evidence and transcripts below. It would be required to overturn factual determinations made and affirmed below that there was no actionable breach of duty by McHale under *any* trustee standard, including the higher standard of a so-called ". . . CPA Trustee . . ." (A. [11a-14a,] 27a).

CONCLUSION

The Petition for Writ of Certiorari should be denied.

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Supreme Court, U.S.
FILED
MAR 22 1993
OFFICE OF THE CLERK

No. 92-1332

IN THE
Supreme Court of the United States
OCTOBER TERM, 1992

CAPTRAN CREDITORS' TRUST, CLUB BAHA, LTD. and TROPICAL PROPERTIES, LTD.,
Petitioners,

v.

DAVID W. MCCONNELL, GERALD A. MCHALE, JR. and MCHALE, EZZELL & CO., P.A.,
Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

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REPLY BRIEF

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REPLY BRIEF

Petitioner will not burden the Court with a detailed analysis of Respondents' factual presentation. Suffice it to say that this presentation is simply shot through with factual errors, as evidenced by the following three examples:

1. Respondents state that "Count II alleged professional negligence against McHale and McConnell" (p. 2). In fact, and importantly, Count II of the Amended Complaint included charges against McHale, McConnell *and* "McHale, Ezzell & Co., P.A."

2. Respondents state that "Contrary to the Petition's attempted implication at p. 3, McHale was not engaged as

a CPA by Club Baha during his tenure as Co-Trustee, neither was the P.A. in any way a Co-Trustee" (p. 6). In fact, the record demonstrates beyond question that McHale had been retained as a CPA by Club Baha (*see* R-1-4 [T]-1398, 1434, 1435, 1536; R-1-4 [TF]-86). In one letter, for example, he conceded that he had been appointed "primarily to act as a representative agent for Tropical Properties, Inc. and Club Baha Limited," and he signed the letter, "Gerald A. McHale, Jr., Certified Public Accountant" (R-1-4 [P]-12, p. 6).

3. Respondents argue that certain closings "were prevented by Grobowsky's refusal to release Club Baha's judgment lien in the state court action" (p. 7 n.5). But the record shows that *McHale* advised Grobowsky and Club Baha not to release the lien, and that even if the lien had been released, no unsecured creditor would have received anything, since two financial institutions had higher priority liens (R-1-4 [P]-43; R-1-4 [T]-1092).

We cite these examples only to demonstrate that Petitioner's recital of the facts was entirely accurate, and that the Court cannot rely upon any part of Respondents' presentation of those facts.

Of more importance is Respondents' treatment of the law. Petitioner has already demonstrated that the District Court misconstrued several of the Bankruptcy Court's key findings and rulings. No further argument is needed on this score, because this Court can read the two opinions and draw its own conclusions. Moreover, little need be said about Respondents' contention that exculpatory clauses in general are not necessarily against public policy. Petitioner has never claimed that they are. Petitioner's position has always been that this particular exculpatory clause, that allows recovery *only* for "proven dishonesty," is so clearly against federal public policy as to require this Court to strike it down.

The one point in the Brief in Opposition that does require further comment, however, is Respondents' contention that the issues in this case, including the legality of the exculpatory clause, are "controlled solely by state law" (p. 12). The Court will note that Respondents do not cite a single case, state or federal, for this important conclusion. The reason is obvious.

First, we would remind the Court of how the exculpatory clause came into play. CRI filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code. Soon thereafter, CRI and some of its largest creditors, including Club Baha and Tropical properties, entered into extensive negotiations, the purpose of which was to satisfy CRI's creditors and to resolve CRI's problems outside the provisions of Chapter 11 and the Bankruptcy Court. The negotiations resulted in the Captran Creditors Settlement Agreement. In 1985, parties claiming to be CCT creditors filed an involuntary bankruptcy petition against the trust. That filing held up the plans to transfer the CCT assets to Club Baha. The Bankruptcy Court ruled that CCT was a business trust and, as such, it could in fact file for bankruptcy. In 1986, CCT consented to entry of an Order converting the case to a voluntary Chapter 11. Club Baha and Grobowsky then proposed a total liquidation plan as the Plan of Reorganization. That plan was confirmed, resulting in an in-kind distribution of the CCT assets to the trust beneficiaries.

It was against this background that the exculpatory clause came into play to absolve Respondents of all responsibility for their acts, which were just short of "proven dishonesty."

Second, the federal courts in this case clearly were not merely substitutes for state courts, blindly bound to follow state law. On the contrary, the cases are clear that issues of bankruptcy are federal questions, and that in particular, state law cannot frustrate or preempt federal bank-

ruptcy policy.[1] "[A]lthough state law governs substantive elements of the claim, its application always remains subject to countervailing federal bankruptcy policy." *Addison* v. *O'Leary*, 68 Bankr. 487, 491 (Bankr. E.D. Va. 1986).

Stated differently:

> While under federal bankruptcy law property rights of debtors and creditors are generally determined by state law, it is also true that where state law frustrates or burdens federal policy, state law must give way. [*In re Schnupp*, 64 Bankr. 763 (Bankr. N.D. Ill. 1986)].

Here, even if state law somehow conflicted with federal policy—and Respondents have not demonstrated that it did—federal policy would necessarily control. A federal court cannot be called upon to perpetrate a miscarriage of justice by allowing trustees in bankruptcy to engage in scandalous activities on the ground that "proven dishonesty" cannot be shown. The prevailing federal policy has to be that trustees in bankruptcy, accountable to the federal courts, are held to a higher degree of care than that.

Therefore, Respondents have helped demonstrate why this case is of paramount federal importance. By contending that state law controls, they have simply pinpointed the fact that federal courts acting pursuant to an Act of Congress—the Bankruptcy Code—cannot be called upon to sanction conduct that clearly violates every precept of federal public policy.

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[1] *E.g.*, *In re: Gambogi* v. *Capodalupo*, 20 Bankr. 587, 588 (Bankr. D.R.I. 1982); *In re: Warren* v. *Warren*, 7 Bankr. 201 (Bankr. N.D Ala. 1980); *In re: Environmental Research & Development, Inc.* v. *Resource Dynamics, Inc.*, 46 Bankr. 774, 775 (Bankr. S.D.N.Y. 1985); *In re: Spanish Trails Lanes, Inc.*, 16 Bankr. 304, 306 (Bankr. D. Ariz. 1981).

The Petition should be granted and the judgment reversed.

Respectfully submitted,

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